

Beyond “Microenterprise Development 101”

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Agenda

- **The case for microenterprise development – growth, poverty reduction**
- **Summary of microfinance best practices and emerging issues**
- **Exercise - Designing a Microfinance Intervention (Fredonia Case)**
- **Making Markets Work for the Poor -- Business Development Services (BDS)**
- **Wrap Up**

Defining Microenterprises...

- Microenterprises are the smallest business activities, often informally organized
- USAID definition: 10 or fewer employees including unpaid family workers; low income and asset levels of owner/operator
- MEs operate in all sectors – services, manufacturing & trade
- “Agro-preneurs” or ‘farm-preneurs”

The Microenterprise Sector Matters...

- **Microentrepreneurs comprise a majority of the economically active work force in most developing countries**
 - **Worldwide:** 64% of employment generated by the microenterprise sector (less than 5 employees)
 - **Philippines:** MSEs employ 55% of the economically active population
 - **Ukraine:** 98% of women-owned businesses are microenterprises
 - **Africa:** Informal sector constitutes 80+% of working population

The Microenterprise Sector Matters...

- **Contributes to Poverty Alleviation**
 - Boosts income of the poor
 - Supports asset accumulation
 - Reduce vulnerability of the poor to shocks
 - Provide opportunities to disadvantaged groups

The Microenterprise Sector Matters...

- **Contributes to Economic Growth**
 - Sector's performance affects economy's overall competitiveness, productivity, innovation
 - Important part of value chain in key national sub sectors
 - Provides affordable products and services to low income groups
 - "Shock absorber", especially in transition countries

USAID and our role in MED

- Leading MED donor worldwide
- Active for 25 years -- well over \$2 billion to date
- Recent funding \$150+ million/year
- Implemented by 60+ Missions
- 700+ implementing partners
- Roughly 2/3 microfinance, 1/3 BDS and enabling environment work

Who is Served?

- 2.8 million borrowers
- 3.5 million savers
- Moderate poor and vulnerable non-poor
- 800,000 poor clients get USAID-assisted BDS
- 67% of clients are women

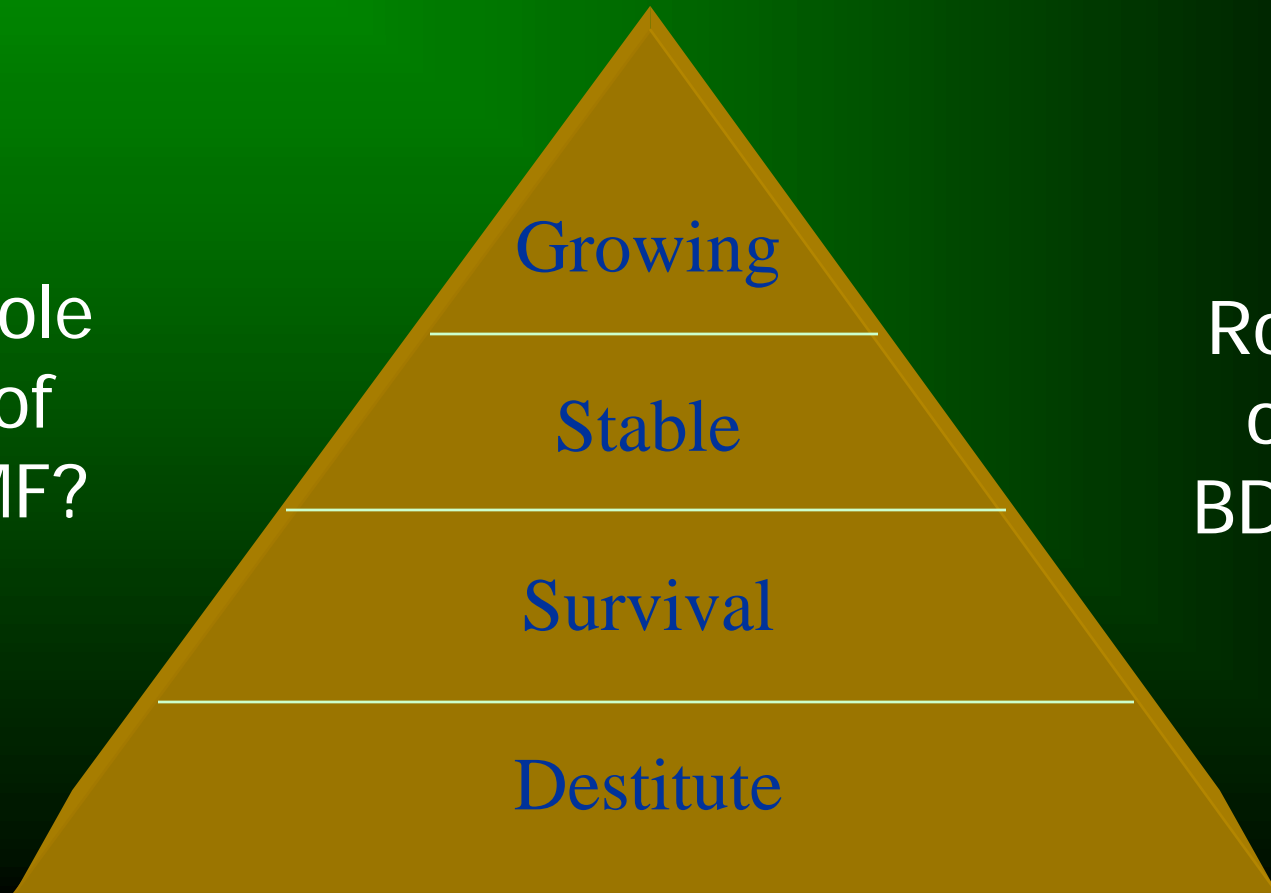


USAID's Approach to Microenterprise Development: The Three Legs of the Stool

Enabling Environment

Role
of
MF?

Role
of
BDS?



Microfinance “Best Practices”

- Summary of best practices worldwide
- Emerging issues in the field
- USAID: What is our role in microfinance development?

Best Practice in Sustainable Microfinance

Ultimate aim = make financial services accessible to the poor in a sustainable way.

- This requires:
 - ✓ MFIs that reach scale & financial sustainability
 - ✓ Commercial sources of capital to finance MFI growth
 - ✓ “Infrastructure” that supports the microfinance market
 - ✓ Policy environment that is conducive to microfinance

The focus should not be solely to build sustainable institutions, but rather a vibrant and competitive microfinance market.

Best Practice in Lending Methodologies

- Solidarity group lending: 3–7 person groups guarantee each others' loans, as substitute for collateral; good for people lacking tangible assets
- Village banking: groups 15+; group administers loans to individuals; women are predominant; good for the very poor and dispersed populations; often combined with health/education/business messages
- Individual Lending: based on analysis of business/household cash flow; usually some tangible collateral or personal guarantees; grows with clients; more likely to be urban

Best Practice in Lending

- Understanding the microfinance client – self employed and microenterprise sector, not the destitute poor
- Non traditional collateral including peer pressure – more flexible substitutes (savings, jewelry)
- Stepped loans as incentive for repayment
- Delinquency management: immediate personal follow up, loan tracking systems that work, no tolerance policy

Best Practice in Lending

- Product Design: small, flexible working capital loans, fit to cash flow of households and business cycle
- Interest rates: set to cover costs for operations and future growth. Sustainable interest rates range from 20 – 100%
- Efficiency: streamline operations for many small transactions
- Separate cost allocation for other non financial services
- Linkages to commercial markets

Best Practice in Savings

- Importance of savings in low income populations: 5 or more savers for one borrower; may be more relevant for the poorest
- The four attributes of successful savings products: safety, convenience, liquidity, return
- Market research necessary for product development; products should reflect savings patterns and client preferences
- Debate – Should there be minimum regulatory requirements for taking deposits from the general public?

Best Practice in Understanding Clients

- Clients use financial services for range of business and household purposes that reflect the business cycle & household consumption
- Clients typically have multiple sources of finance and use of finance
- Indicators such as desertion or drops outs alert MFIs that clients aren't getting what they want
- Let's meet Juanita

The World According to Microcredit Institutions and Their Donors



The World According to Juanita

Microenterprise

Emergencies

Education

Housing Improvement

Consumer Goods

Celebrations/
Vacations

Basic needs: food,
clothing, medical

Old age pension



Appliance store

Western Union remittance

Credit union or state bank
savings account

MFI loan

ROSCA with friends

Money lender

Cow, chickens

Pawn Broker

Microenterprise income

Uses

Sources

Range of Institutional Models

- NGOs
- Transformed NGOs
- Commercial Banks
- State Banks
- Credit Unions
- Savings and Loan Cooperatives
- Consumer lenders
- Financing companies
- Appliance stores

The Role of USAID in Microfinance

Steps to designing a strategy...

Step 1

Perform Market Assessments

- What's the client profile? Who's left out?
- What products and services are available?
- Who are the main players in the market, including NGOs, commercial banks, and other institutional types.
- What percentage of the economically active poor are being served by microfinance?
- How does the legal and regulatory environment look – is it conducive to a competitive micro finance industry?

Steps to designing a strategy...

Step 2

Identify how mature the microfinance sector is in your country

- Early Phase: Few institutions, low outreach, standard product, best practice microfinance is not predominant
- Expansion Phase: More MFIs in the market, increased outreach, focus on operational and financial sustainability
- Competition Phase: Sustainable MFIs, commercial actors enter market, new products, reaching more underserved markets
- Mature Phase: Mergers, clear market leaders, growth tapers and movement up market

Steps to designing a strategy...

Step 3

Identify the other actors

- What are other donors doing? Potential for donor coordination, avoid sending mixed messages
- What is the role of government, central bank?
- Is there a microfinance network or association, what are they doing?

Steps to designing a strategy...

Step 4

Select intervention that makes sense based on country context

- Range of options:
 - ✓ Grants to new entrants
 - ✓ Loan Capital
 - ✓ Capacity building
 - ✓ Support to policy work, including support to regulators
 - ✓ Support for micro finance associations
 - ✓ Credit Guarantees
 - ✓ New product development
 - ✓ Support for credit bureaus
 - ✓ More...

<p>Early</p> <p>Countries like: Nigeria, Brazil, Afghanistan, Azerbaijan, Congo</p>	<p>Awareness raising, grants to new entrants, policy, training, industry-wide capacity building</p>
<p>Expansion</p> <p>Countries like: India, Georgia, Egypt</p>	<p>Loan capital to lead MFIs, new players, technical assistance (internal controls, MIS, management), support for microfinance associations, policy</p>
<p>Competition</p> <p>Countries like: Bosnia, Uganda, Nicaragua</p>	<p>New product development, reaching rural and underserved markets, assist to leverage commercial capital (DCA), regulation and supervision</p>
<p>Maturity</p> <p>Countries like: Peru, Bangladesh, Bolivia</p>	<p>Policy, commercialization support, creation of credit bureaus, collateral law, consumer protection,</p>

Steps to designing a strategy...

Step 5

Match Mission Interests and Resources

- Match interventions with SO priorities and indicators
- Match interventions with budget and time frame
- Determine staff resources available to manage a complex micro finance portfolio
- Consider staff training in best practices microfinance

Steps to designing a strategy...

Step 6

Design Program with appropriate objective and meaningful indicators

- Determine the need for market assessments required before RFA/RFP issuance
- Determine mechanism that makes sense given funding level (Consider AMAP IQC for Financial Services)
- Develop RFP/RFA that requires best practices and promotes innovation
- Set appropriate targets, refer to resources such as Microbanking Bulletin & MD Office "Table 1"

Steps to designing a strategy...

Step 7

Monitoring & Evaluation

- **Signs of success include:** MFIs exceed performance targets, improvement in financial sustainability, competition emerges, policies more conducive, increased commercialization, innovations and products and services in the market
- **Signs of failure include:** No client growth, high delinquency, no entrants into the market, policies that limit the growth of the industry, no innovation in products and services, corruption

Microfinance Case Study

Fredonia

Emerging Issues in microfinance

Reaching rural clients:

- There are financially sustainable MFIs in many countries, but they are mostly in urban areas with high densities. The very poor often live in rural areas and are linked to the agriculture sector. How can microfinance reach the rural poor and those working in agricultural-related activities?

Refugees, Internally Displaced Persons (IDPs) and Post Conflict:

- Violence and unstable political condition increase number of internally displaced people in capital and secondary cities and certain geographical areas. Recently displaced people lack formal collateral – Can microfinance work for this target group? What needs to be done differently?

Emerging Issues in microfinance

Savings and New Product Development:

- Increasing number of poor have access to microcredit, usually short term working capital loans. Little or no access to other products such as savings, insurance, money transfers, housing and home improvement loans, etc. How can microfinance address those needs?

Access to Capital Markets:

- Mature microfinance industry with strong MFIs in the market. Access to commercial capital is a challenge, potentially affecting growth. How can mature MFIs finance growth? (commercial sources, deposits, retained earnings)

Emerging Issues in microfinance

Market Infrastructure

- What are appropriate interventions to support more mature, competitive microfinance markets with diverse, strong MFIs and clients? What about credit bureaus, collateral law/registry, more...

Policy Changes:

- What are the minimum legal and regulatory conditions that need to be in place for microfinance to develop? How do these conditions need to evolve as the industry matures.

Making Markets Work for the Poor

Revisiting Business Development
Services

Agenda

- What is BDS?
- Case Studies
 - Bangladesh, India & Azerbaijan
- Emerging Good Practices in BDS
- USAID Missions, what is our role in business development services

Common Myths about BDS

BDS is not just training

Common Myths about BDS

BDS is not affordable to the poor –
it needs to be subsidized

What is BDS?

Market Linkages, product development,
production training, technical assistance...

Services that help MEs:

enter and meet the requirements of
new markets

What is BDS?

Improved input services, accounting services, business training, advisory services, ICT, courier services...

Services that help MEs:

increase their efficiency/lower costs

What is BDS?

Business planning, financial analysis, tax services...

Services that help MEs:

apply for loans and comply with regulations

Best Practice in Sustainable BDS

- The ultimate aim of BDS is to increase the incomes of micro and small enterprises through – for instance - improving access to markets, developing market-tailored products, and increasing the quality of products.
- Develop commercial business service markets so that micro and small enterprises have sustainable access to services that enable them to grow.

Bangladesh (JOBS Project): Outsourcing to MEs

Pre- Outsourcing Situation:

- Growing footwear sector, small # exporters
- Exporters cannot fulfill orders, limited production capacity
- Contract basis initially, cannot predict work flow
- Cost of hiring full time employees too high
- Large number MEs working in footwear production for local market
- Potential source of flexible capacity
- Interest to enter new markets, value added products
- Unfamiliar with market demands and requirements

Is there a win-win solution that increases competitiveness and benefits micros?

Bangladesh (JOBS)

Techniques to work with “micros”

- Help micros form clusters through tender
- Help exporters to provide services (raw materials, training, quality control, machinery, etc) so that ME clusters can perform
- Help exporters to penetrate new markets, plus technical assistance in product development and quality control

Bangladesh (JOBS)

Win – Win Approach

Export Firms

- Flexible capacity, can meet orders on time and can fulfill orders
- Inter-firm collaboration allows for stronger industry cluster
- Competitive advantage, can compete in world markets
- As of May 2002, 244 micros are linked to footwear sector for export markets

Microenterprises

- Can sell in domestic & export markets
- Higher quality products (value added), higher prices
- New skills, access to market information
- Not tied to one exporter, can subcontract to any export firm (leverage)

Azerbaijan

Market Access for the Very Poor

Situation:

- Very poor, women in poultry business (\$34 monthly)
- Price is low
- Rejections by the State Animal Health Board due to poor quality feeding and breeding
- Unaware of preventive services that could keep poultry healthier
- Veterinarians are available in the market, but do not view this market segment as viable, "the poor cannot afford"
- No economies of scale due to large distances between villages

How can "micros" sell at better markets?

Azerbaijan

Techniques to work with “micros”

- Awareness campaigns to illustrate the benefits to preventive vet services
- Formation of groups that collectively purchase preventive vet services
- Make the BDS affordable – Monthly savings fund (insurance) that finances periodic vet visits
- Vet Network – share cell phone costs, similar to a taxi dispatch service
- Diversify services – work with a number of vets to diversify services, emergency & preventive services; bundle services

Azerbaijan

Win – Win Approach

Poultry MEs

- Micros have access to reliable BDS services, including access to better markets
- Increase quality of poultry, less rejection at State Board
- Projections – 7000 micros will increase sales by 35%
- No longer selling in black market

Vets

- Tap a new market for both emergency and preventive services
- Projections – 90 vets and vet suppliers increase profits by 87%

India (ITC Ltd's e-Choupals)

Backward Integration to Rural Poor

Pre Backward Integration Situation:

- ITC, Ltd, leading Indian retailer (+2 US Billion Sales)
- Difficulties sourcing commodities, quality is low, volume is low
- Penetrating rural, low-end markets – clients are not interested in their products
- A large portion of India's 150 million hectares of agricultural land is managed by small holders, fragmented
- Small holders rely on intermediaries to sell products, low prices
- Limited access to best practice farming and info
- Unfamiliar with benefits of improved agricultural inputs

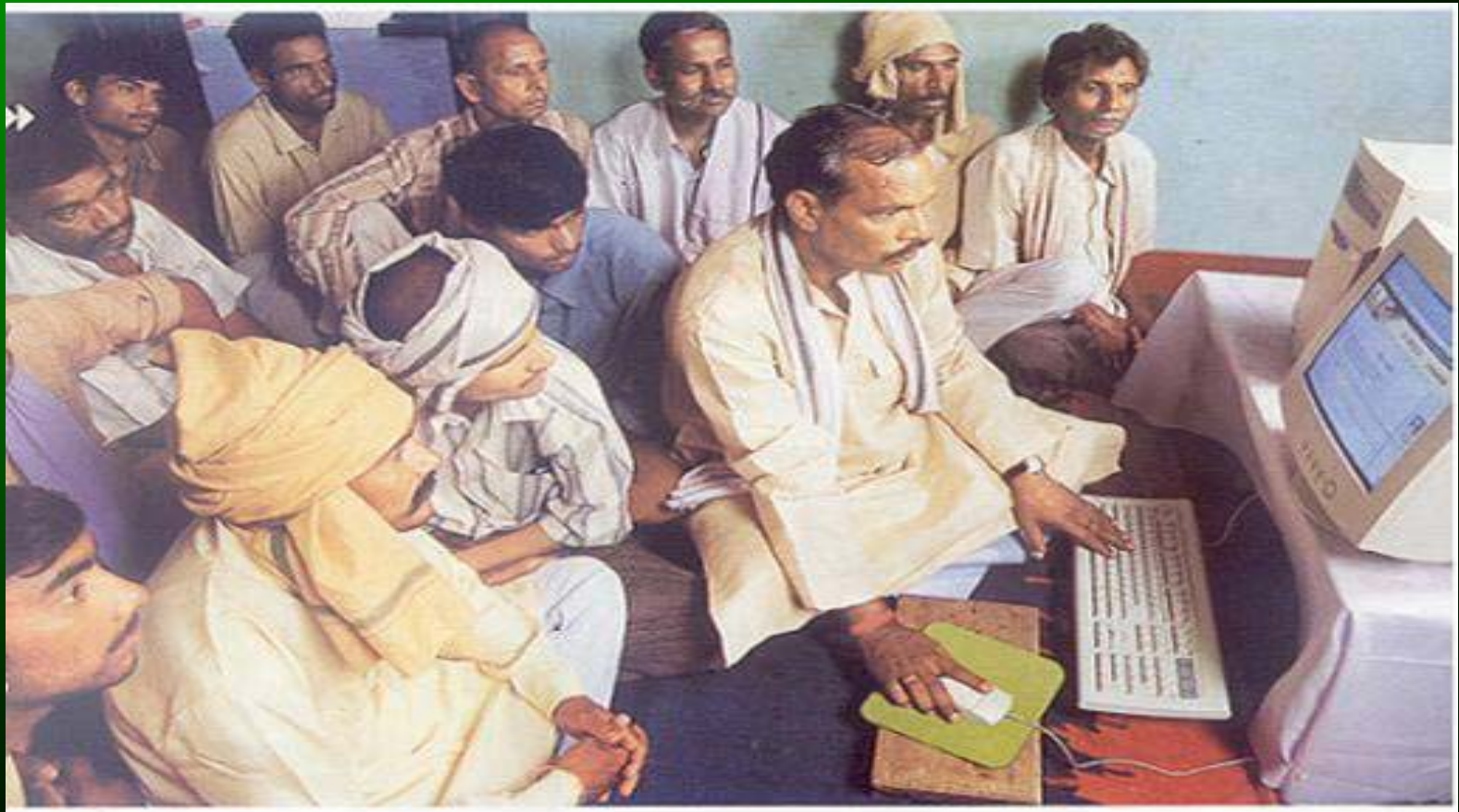
How can ITC tap small holders market in India?

India (ITC Ltd's e-Choupals)

Techniques to work with “micros”

- Internet connected kiosks, known as e-Choupals – provide latest weather reports, local and international produce prices and farming best practices
- Lead farmers (Sanchalaks) – have commercial incentive to promote use of e-choupal
- Common collection points (e-choupals and ITC storage hubs) allow farmers to consolidate orders
- One stop shops - Allows micros to sell products and purchase inputs easily, advantages of bundling services
- Brand recognition, demand creation

E-Choupals at work



India (ITC Ltd e-choupals)

Win – Win Approach

ITC Ltd

- Targeting US \$400 million in international exports by 2005
- Cost savings in commodity sourcing
- Distribution channel for variety of goods and services, more sales

Microenterprises

- Currently 1,286 kiosks, reaching 1 million farmers
- Increased revenues to farmers; enhanced yields, improved procurement; marketing and distribution
- Access to more products and services - crop diagnostics, small loans

Good Practice in BDS

Lessons to date

- Micros can be mainstreamed into the economy – can be linked to growth sub sectors and are consumers of goods and services
- BDS can reach the poor:
 - ✓ Provide services along the supply chain (embedded in the sale)
 - ✓ Make BDS affordable -- groups, payment schemes that match cash flow
 - ✓ Understand demand patterns – brand recognition; demand creation; cultural and gender considerations
 - ✓ Bundle services; one stop shopping

Good Practice in BDS

Lessons to date

- Market access and market information are key BDS services that micros demand
- BDS services can be provided by a wide range of providers – private sector firms, firms along the supply chain, ngos, chambers of commerce, associations and more
- BDS can be provided in a sustainable and commercial manner; BDS providers are marketing their services/products differently and using cost effective techniques
- BDS has the potential to reach large impacts over the long run

Good Practice in BDS Program Design

- Select BDS service markets that specifically address constraints at the micro level and that lead to economic gains
- Facilitate the market, don't distort the market

Supply Side

- ✓ Market research to identify opportunities in the market
- ✓ New product development
- ✓ Work with a number of firms offering business services; promote competition

Demand Side

- ✓ Demonstration activities to create demand
- ✓ Facilitate the formation of groups, networks, clusters

Good Practice in BDS Program Design

- Allow the market signals to develop; avoid subsidizing the services directly
- Build local capacity to provide services in the long run; programs that provide services directly may crowd out the private sector
- Foster a level playing field – work with a number of BDS institutions, in particular those with cost structures appropriate for smaller transactions

What's important about this new approach is that it aims to ...

Go one step further than your typical private-sector development programs by

intentionally developing and making sustainable the support services needed to grow businesses over the long run

USAID Missions in Action

- USAID Kenya SO 7 Increase Rural HH Incomes

Summer 2000/01: Investment in BDS Training

Summer 2001: Evaluation of Past BDS Activities
Market Assessment (Sub sector focus)

Fall 2001: Strategy Development – Good practice
BDS

Spring 2002: Draft RFP – Require innovative ways to
work with micros; build BDS markets;
and sustainable impacts; limited direct
service provision

November 2002: Contracted
STTA Unit in Place – BDS Training for all
contractors under SO 7 – Rural Household
Incomes Increased

USAID Missions in Action

- USAID Bangladesh SO 5 Growth of Agribusiness and Small Business

Fall 2001: BDS Assessment

Spring 2002: Evaluation of Past BDS Activities (JOBS)
Case Study

Summer 2002: Donor Collaboration; Gemini Survey,
Review of Sub Sector Studies
Investment in BDS Training

Fall 2002: Draft RFP; Require innovative ways to
work with micros; building BDS markets;
and sustainable impacts; no direct service
provision
Considering AMAP Mechanism

Challenges in Working with Micros

- **Micros are in weak market positions in value chains** – cannot negotiate better prices; are in monopolistic relationship; do not have access to market information
- **Micros are locked in certain sub sectors & products** – cannot easily jump into other sectors if sector declines; forced to compete for price
- **Micros consider risk and vulnerability in their business decisions**

Microfinance + BDS +
Enabling Environment =
Microenterprise Development

**Wrap-up and
How We Can Help?**

Comprehensive MED Strategy

Working at All Four Levels:

Policy

Service Market

Service Providers

Clients

The Enabling Environment– Burning Issues and Responses

- Severely uneven playing field for informal sector and MEs
- Legality, feasibility and attractiveness of microfinance
- Problematic policies affecting key ME sub sectors, E.G., Tourism, Agroprocessing

Enabling environment

Lessons to date

- Look for ME-specific issues but often best to address within broader MSME initiatives
- Enabling environment reform needs to be tailored and locally-owned, using local advocates, NGOs, researchers
- Facilitating linkages among MSMEs is very powerful, no cookie-cutter approach
- New laws are not enough, focus on implementation too
- Demonstration and ripple effect –more impact

Examples: Zambia, Nepal

Zambia

- AMIZ (Association for MFIs in Zambia)
- With local legal drafters, the GOZ and Zambian advocates developed a tiered system of MF regulation & supervision
- Broad coalition
- Three draft bills in Sept 2000
- Training in implementation of the law in process

Nepal

- Property rights for women is a key constraint in MED
- National effort to rewrite property rights legislation for women, in collaboration with all major women's rights organizations, Parliament and donor agencies
- March 2002 – Bill was passed

What's on the Horizon?

- Legislation and poverty concerns
- Relationship to new AID priorities -- TCB, agriculture, conflict
- Using the DCA tool
- Millennium Challenge Account

MD Services

- Our field support goal: to help Missions start, expand and improve their microenterprise programs. For example, assistance with:
- developing SOWs for BDS and MF market assessments
- developing RFPs and technical review/selection
- evaluating and retooling existing programs
- financing market research, implementation, evaluation

Resources Available

- Brand-new IQC for comprehensive contracted technical services (AMAP)
- Funding -- PRIME co-financing Program, training scholarships
- MD staff support
- Training and staff development
- Information and communications
- Information Packet (Today)

Thank You!

Questions?